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ABSTRACT

This guide, designed primarily to assist school administrators, describes programs initiated by school districts to finance new school construction by nonconventional methods. Accompanying the basic information are case studies and charts illustrative of major financing alternatives and the decisionmaking routes that have led school districts to adopt one approach or another. (Author/MLF)

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Guide to alternatives for financing school buildings

A Report from Educational Facilities Laboratories

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Foreword

In the good old days of the soaring sixties it was natural to place importance on design and planning to improve the quality of educational facilities. The concern with design and planning was tempered by the realities of construction costs, but nevertheless it was assumed that money was available for school and college buildings. Now, in the sagging seventies, the priorities are rearranged so that getting money together has become a prime concern for most educational administrations.

EFL believes its role in improving the facilities for education also includes helping administrators to understand the options for financing facilities. So, it commissioned Gary Stonebraker, president of the Advanced Planning Research Group, Inc., to develop this guide. Stonebraker was assisted by a committee of EFL consultants who are listed in the appendix.

Although the material in this publication conforms to customs and laws in some parts of the country, its recommendations are not applicable in all parts of the U.S. Readers should check carefully before assuming they have found a solution to their districts' particular problems.

Educational Facilities Laboratories.

Introduction

Now that the post-war "baby boom" has had its full impact on school districts across the nation, school-age population may stabilize in many districts, and in some it may even decline. This may suggest that the worst school building problems are over, but nothing could be further from reality. The recent great demand for new school construction in growing areas has forced many school districts to overlook maintenance and modernization of old schools. These school districts now face staggering problems in replacement or renovation of schools. And, continuing population shifts force continuing changes to schools in cities and suburbs. Also, many of the hastily-constructed schools of the nineteen-forties and fifties did not anticipate the changes in education, and therefore are obsolete for all practical purposes. So, for these reasons the demand for new school construction, or for modernization and replacement of existing schools, will not ease significantly in this decade.

Can school districts meet this demand? The single, overriding factor will be the ability of school districts to *finance* new construction. And on that issue, many school districts are in deep trouble. In many major cities, the capital outlay programs for schools are nearly bankrupt. Many school districts have used up their legal capacity to support long-term financing of new construction. In nearly half the bond elections, voters are refusing to support new taxes to pay for new school construction; and at least one major city has not had a new bond issue of significant size in a decade. State aid programs are not often able to help in significant ways; and of course, at this time, there are no major federal programs supporting construction of elementary and secondary schools. As a result, many school districts —perhaps the majority of school districts— are seriously behind in school construction and have little hope of getting the financing needed to catch up.

But necessity is indeed the mother of invention in these circumstances. Some school districts under great financial pressures have developed original and inventive ways to get schools built, to obtain new sources of financing, and to better manage their fiscal resources. As these methods have emerged and gained national attention, EFL has received an increasing number of inquiries about them.

Although EFL's main concern is with the facilities of education, it also recognizes that sound planning and design depends upon sound programs of financing. On too many occasions good school plans have been stripped of quality and character because the facility could not be financed. So, unless the present fiscal crisis confronting school districts is resolved, tomorrow's schools will be far short of our abilities, talents, and aspirations—if they are built at all.

In this guide, EFL presents basic information on how school districts are financing new construction outside of conventional methods. Some of these ideas may be applicable to your local school building programs. To help determine this, the information is accompanied by a chart that illustrates some major financing alternatives, and the routes of decision-making which have led school districts to adopt one approach or another.

Although all the alternatives discussed have been legally used by one or more school districts, laws vary widely from state to state. Specific alternatives may not be legal in your state. The only way to be sure is to consult your legal counsel, or to seek the advice of state school authorities or the state attorney general. EFL does not advocate or endorse application of any of these ideas.

1 Pay-As-You-Go Financing

Pay-as-you-go simply means that a school district pays cash for all construction. Cash can be obtained through:

—One-time levies approved by voters at referendums.

—Accumulation of money in reserve funds.

Many school districts depend upon grants or other sources of cash to supplement local cash. Some additional methods of raising cash are discussed in Sections 2, 3, 4, 5, and 6. These methods may be used in various combinations to raise a maximum of cash, thus minimizing the amount of long-term financing required.

1a Can you pass a one-time levy for school construction?

Under most normal circumstances, voters can decide to tax themselves on a one-time basis for public projects. This can be done on a district-wide basis or within "special assessment" districts formed for particular neighborhoods or taxing units.

At one time, such levies were a predominant form of paying for public construction. However, as school size and cost increased, and as long-term financing became more available and acceptable, the use of one-time levies declined.

These levies are criticized because they burden the taxpayers at one point in time, while future taxpayers may pay nothing for school construction. Because of this, long-term financing may be preferable because it spreads the burden evenly among taxpayers over time. On the other hand, long-term financing requires payment of interest charges that can add from 40% to 200% to the cost of school construction.

Pay-as-you-go avoids such charges. But the size of levies required for today's school costs create a formidable proposition on the ballot. Experience shows that such propositions are highly unlikely to succeed.

1b Can you accumulate money in a sinking fund or reserve fund? 7

Reserve funds are used by private corporations to accumulate money against inevitable future expenses. For example, a manufacturing company may accumulate money in a fund to replace a plant when it becomes obsolete. For these purposes, depreciation of the plant is budgeted as an expense and the money for paying that expense goes into the fund. The advantage is that the money earns interest while accumulating, and when the equipment is replaced it can be paid for in cash. This avoids long-term financing charges.

Some government planners and economists assert that it would be sound management to use these funds for public projects such as school construction. However, for a variety of reasons, such funds are illegal in many states. One practical reason is that it is thought imprudent to collect taxpayers' money and earn interest on it when the taxpayers could be doing the same.

However, there are states where the funds can be legally used to set aside money for school construction. These funds may be preferable to one-time levies if pay-as-you-go is the objective, since the burden can be spread more evenly among taxpayers over time. However, the fact that such funds accumulate interest and avoid finance charges may not always represent an economy. Where construction costs are escalating consistently and rapidly, it may be more economical over a long period to seek long-term financing.

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2 State Aid

State aid programs have grown in usage and scope since World War II. Two forms predominate: Grants-in-aid, which are gifts from state to school district to supplement local funds; and state loan programs, which provide loans for construction in lieu of selling bonds on the open market. For loan programs, see section 7. For states operating grant programs, see section 2A. These listings were obtained from *Financing Public Elementary and Secondary School Facilities in the United States,* published in 1970 by the Indiana University School of Education, Bloomington, Indiana. This document provides an excellent overview of these programs across the country.

The details and scope of state-aid programs vary too widely to explore in this publication. However, few programs provide 100% of funds needed to finance school construction, and those that can provide 100% funding may do so only in highly unusual circumstances. In general, the programs must be regarded as supplemental to local funds.

2a Does your state operate a grant program?

These states issued school planning and construction grants in 1969:

Alabama (in millions)	$ 1.9	Kentucky	$ 20.8	North Carolina	$ 8.4
Alaska	1.6	Maine	4.0	Pennsylvania	50.0
Connecticut	16.0	Maryland	50.5	Rhode Island	4.1
Delaware	15.6	Massachusetts	23.7	South Carolina	16.4
Florida	56.4	Mississippi	6.6	Tennessee	10.4
Georgia	28.3	Missouri	1.8	Utah	4.2
Hawaii	30.3	New Hampshire	2.9	Vermont	4.6
Illinois	1.9	New Jersey	28.6	Washington	13.0
Indiana	46.6	New York	184.0		

2b Can you qualify for a grant?

Wide variations in program requirements and purpose make it impossible to give specific advice on qualification for state grant programs. However, in some states, grants are made only to districts unable to support additional bonded indebtedness. This may include districts that have reached their legal debt limit; cannot pass bond issues; or cannot market bonds. In the latter case, state loan programs may apply (see sections 7C, 7D). Some special-purpose grants are made for particular purposes or types of facilities.

For additional information: Case Study C
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3 Federal Aid

At present, the only major federal assistance program giving funds directly for school construction is administered by the U.S. Office of Education, Division of School Assistance for Federally Affected Areas, School Construction Branch, Washington, D.C. Other federal programs, however, offer indirect aid for site acquisition, planning and other special uses.

A federally affected area is one in which the presence of government installations adds children to the school rolls. Because the federal government does not pay local property taxes, it provides "impact aid" to help support local schools.

Under the impact aid program (Public Law 815), school districts that have a 6% increase in federally related student enrollments over a four-year period may be eligible for a grant-in-aid for school construction. Federally related students are children of federal employees or military families, or children of families living on federal lands. The size of the grant is determined by the number of federally related students added during the increase period, multiplied by the established per-pupil construction cost in the state. Several additional criteria apply, and fund limitations may delay the grants. Additional details are obtainable from the program administrators.

For additional information: Case Study K

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4 Reducing Site Costs

Acquisition and preparation of a site forms such a large part of a capital budget that if the site costs can be eliminated or reduced, the total construction cost of a school can be lowered between 10% and 25%, depending on the value of the property. However, as the following examples show, school districts may be unable to accomplish this except in unusual circumstances.

4a Is the school site on urban renewal land? Can you get a "free" site by using urban renewal credits?

Within a city's declared urban renewal area, land may be bought and cleared by a joint (25%-75%) contribution of city and federal funds. The cleared land is then "written down", i.e., sold at a lower price to make it economically feasible to use the property for housing, etc. The federal government provides 100% of the working capital for such projects; the city pays its 25% share only as the land is sold. However, the urban renewal laws stipulate that if the city re-uses urban renewal land for certain public purposes, including school construction, it will receive a "credit" for its share of the cost of such property; this credit relieves the city of paying its 25% share. Thus, the school district can acquire "free" school sites within urban renewal areas, and can avoid site acquisition and clearance costs.

4b Can you avoid site costs by building on air rights over other public property?

Because public land within a city produces no tax income, planners seek to multiply the use of existing public land so that no further private land will be taken off the tax rolls. In accord with this, some school districts are exploring the possibility of building schools over the "air rights" of freeways, transit lines, etc. Although this avoids the cost of site acquisition, construction may cost more since air-rights buildings usually require long spans and heavy construction, and may pose special problems such as isolation of noise and vibration.

In a related example of land use, the Dade County School District (Miami, Florida) proposes to build a school under an elevated freeway, on land technically owned by the federal government. The land will be leased to the school district for a nominal sum.

For other possible uses of air rights, see section 6B.

For additional information: Case Study B
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5 Shared Facilities

In many cases, school districts and other community agencies build and operate separate facilities which are nearly identical in character. For example, a school library is often similar to a branch public library. School health clinics may be similar to neighborhood community health facilities. Physical education facilities may be similar to facilities operated by the Parks and Recreation Departments. Where separate facilities are built and operated by two agencies, each may be underused. For example, branch libraries are often empty during the day, while busy during evenings and nights. School libraries may be the opposite.

Where such conditions exist, public agencies and the taxpayer may both benefit by joining together to build a common, shared facility. This can be done in three ways. First, the school district can build the facility and lease it to other using agencies. Lease income can be used to offset capital and operating expenses. While this does not benefit the school district financially, it does benefit the city by avoiding the cost of duplicate facilities. Second, the school district can ask the second agency to build the facility in conjunction with a new school. This reduces the capital cost of a new school district. This is particularly attractive to school districts with tight capital budgets. Still another option is to share first costs based on expected *pro rata* usage (see section 5B).

5a Can you find other agencies that are willing to share facilities?

Check agencies at city, county, state and federal level. City prospects may include:
—Health programs needing clinics or diagnostic screening facilities
—Recreation programs to share gymnasiums and playfields
—Day care agencies and Head Start groups to share facilities with lower grades in elementary schools
—Job training or vocational training programs which might use shop and other similar facilities
—Adult education programs, including those run by private institutions, that might use school space after hours
—Municipal libraries that might share school library facilities
—Local arts and crafts groups, hobby clubs, and other groups that might lease facilities.

At the county and state level, check these prospects:
—Local junior or community colleges
—State-run technical education and vocational training programs.

At the federal level, certain kinds of grants-in-aid may be available to support community facilities. In at least one case, the Department of Housing and Urban Development provided grants-in-aid for construction of community facilities within a school complex, where the school was able to share those facilities.

5b Can you work out a cost-sharing formula?

The type of cost sharing formula to be used is a matter of preference for the agency involved.

One method is to share the "first costs" of the facility on the basis of prorated usage. First cost in this case would include not only construction costs and related fees, but also interest paid on the facility.

If the first cost is $100,000, and the school system is expected to use it 36 hours per week while Agency X uses it 12, then Agency X might pay $25,000 (12/48) while the school pays $75,000 (36/48).

Where the facility is part of a larger structure, it may be difficult to allocate construction costs for that particular facility. Similarly, it is also difficult to determine a fair share of maintenance and operating costs. In these cases, a cost sharing formula may be difficult to agree upon.

A second method is for one of the sharing agencies to agree to finance the total facility, and to lease or rent it to the other agency on a usage basis. An "hourly-cost" formula can be agreed to in advance. For example, a facility costing $100,000, including debt service, is to be amortized over 15 years. The school will use it 36 hours per week, and Agency X will use it 12 hours per week. With a 36-week school year, the use in 15 years will be:

—48 hrs x 36 wks x 15 yrs = 25,920 hrs

and the average hourly use cost could be estimated at:

—$100,000/25,920 hrs = about $4.00/hr

exclusive of maintenance and other costs. Similar formulas may be applied to annual maintenance costs.

A third way to develop such facilities is for one agency to build the facility, and simply give another agency the right to use it. One agency thus avoids all costs; and the local government benefits by avoiding the cost of duplicate facilities.

For additional information: Case Studies F, K

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6 Non-tax Revenue

School districts unable to raise money through more conventional methods have discovered that school-owned land is a valuable commodity which can generate additional income. Some districts have sold or exchanged land to get cash for building. Others have sold or leased ground rights and air rights over school property. Still other school districts propose to build rentable space in conjunction with school facilities as a means of offsetting construction costs.

All of these methods pose special legal and political problems for the school district. Use of these methods should be considered only on the advice of legal counsel, and only after careful testing of local opinions.

6a Can you legally sell or exchange property for gain?

School districts may hold properties whose value has increased over time. For example, urban school districts may find that center-city properties are in the path of commercial or other development. Suburban and rural school districts may hold land adjacent to commercial properties or land wanted for residential development. Such land can be sold and part of the income used to buy less valuable but equally usable land elsewhere.

There are several ways in which this might be done. First, the property can be sold outright. This usually requires open competitive bidding. Second, the school district can lease ground rights on part of the property to a developer and retain part for school use. Such a lease gives the lessee rights to build on the property. The lease income may be used by the school district to help pay for construction. Third, the district can exchange property with other public agencies that may need the school's land. In one unusual case, the rate of exchange was such that the second agency provided land complete with a new school building in exchange for the district's property.

If land cannot be sold, its air rights may be leased (see section 6B).

6b Can you sell or lease air rights over school property?

The air rights to a property are, literally, the rights to occupy the air space over the property. The right to sell or lease air rights is well established for private property owners. Several school districts, mostly in urban centers, are selling or leasing air rights and using the income to offset construction or site acquisition costs.

Typically, a school district sells air rights in a densely developed area where privately-owned high-rise development is economically justifiable. The air-rights owner or lessee then constructs an office building, apartments or other commercial property. The commercial portion of the project is taxable, which provides additional income to the city.

In some cases, the air rights building may be in a separate structure adjacent to the school. In other cases, the school structure is underneath the air rights building. In the latter case, the school is more expensive to build than if standing alone, and the air rights developer may be asked to share these added costs. The cost-sharing formula in such cases is usually based on estimates of the difference between (1) actual school construction costs, and (2) estimates of costs for the same school without the superstructure.

Theoretically, it would be equally possible to use air rights in reverse for school construction. For example, a school might lease ground rights for the construction of commercial property (see section 6A), while reserving the air rights for construction of school space over the commercial property. This might be feasible where commercial high-rise construction was impracticable but where other commercial development was feasible (e.g., a shopping center). In order to be worthwhile, the ground lease income must offset the added cost, if any, of constructing the air-rights school.

If a school district has legal or managerial problems implementing such schemes, it may be useful to explore these ideas in conjunction with leasing through a non-profit corporation created for the purpose (see section 8D).

6c Can you legally and profitably rent space in a school building?

A school district may be able to capitalize on the commercial value of its property by building rentable space in conjunction with its schools. Such "joint tenant projects" might house other public agencies or private enterprises, such as stores and cinemas. These ventures are most valuable in offsetting annual costs, because the initial capital outlay will be greater.

Building space to rent is both a politically volatile venture (because of competition with private interests) and an economically risky proposition. It should be approached only with the advice of legal counsel and a real estate investment counselor who can prepare detailed analyses of economic feasibility. Also remember that code requirements for joint-occupancy structures may be stiffer than for single-occupancy, separate buildings. This can make construction costs higher.

If such a scheme is not possible but the idea of joint occupancy remains attractive, you may investigate leasing of ground or air rights to a private developer for the construction of the commercial properties (see section 5A, 5B, 6B).

For additional information: Case Studies A, C, F, H
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7 Bond Issues

General Obligation Bonds, the traditional medium of long-term financing for school construction, are legal in all states, but their use and sale is heavily regulated.

GO financing covers site acquisition and improvement costs, planning costs, and the construction of new school facilities, additions, and major renovations. Several projects may be built under one issue. The total amount of the issue must be estimated carefully.

The school district must then determine whether it can legally issue bonds in the amount required. This is controlled by the debt limit (see section 7A), and the bond market (see section 7G). If favorable, the bond proposal is drawn up, and a bond election called that authorizes the school district to market the bonds and to raise taxes if necessary to pay for them.

If the issue passes, the school district sells the bonds to obtain the cash to pay for project costs. These sales take place at an advertised bond sale at which bidders propose to buy part or all of the bond issue at a bid or negotiated interest rate. Sales are awarded to the combination of bidders providing the net lowest cost to the school district, providing that all bids are within the legal interest rate governing the school district.

Two types of bond issues are used. In a term issue, all bonds mature at a given time. Where legal, income tax monies may be held in interest-bearing reserves (sinking funds) until the bond issue matures. If interest earned exceeds interest paid, it will reduce the cost of the bonds.

The second type, serial issue, is currently the most popular. Serial issues have different quantities of bonds maturing at different times. They can be planned so that the amount redeemed in a given time period, plus the amount of interest paid on the remaining bonds, is equal in all time periods. This permits better long-term fiscal planning geared to expected tax income.

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7a Can you legally assume more debt?

The bonding capacity of a bond-issuing jurisdiction is usually limited by state law. Limits are commonly set by the assessed valuation method. This sets the total indebtedness of a jurisdiction as a fixed percentage of the assessed value of taxable real estate within the jurisdiction. The intent of the restriction is to limit the total debt to an amount that can be paid off by future property taxes, which vary directly with assessed valuation.

There are several difficulties with this system of limiting debt. First of all, it tends to favor highly-developed areas with high concentrations of commercial and industrial properties that are assessed at higher rates and produce higher tax yields. Rural and suburban areas without such concentrations cannot assume as much debt per capita as urban areas. But these less-dense areas may be in greater need of funding, especially where they are growing rapidly.

A second disadvantage of the system is that assessment procedures are not uniform in all areas. While assessment rates may be uniform (e.g., a fixed percentage of market value), the procedure for setting the market value itself may vary. Such assessments usually depend on the tax assessor's judgment (or preferences). This results in wide discrepancies between the reported tax bases of communities and their real worth. Such discrepancies can lead to high bond interest rates, since the community does not properly represent the real collateral backing bonds.

A third disadvantage is that no allowance is made for future growth in particular areas. Rapidly developing areas may see their tax bases double or triple in the next decade, and accordingly, their ability to repay will grow rapidly. Where this is clearly the case, it might be better to take advantage of today's lower costs and build in advance of such development. However, this is not possible because the debt limit is determined by the present tax base. Therefore, growing areas lag in providing public facilities, since the development generating the need must take place before the community acquires the tax base to satisfy the need. Some states provide appeals procedures for obtaining special exceptions to the debt limits. This may allow growing communities to issue more bonds. (See section 7B.)

When the total long-term debt of a bond-issuing jurisdiction equals the limit set by the assessed valuation rules, the community reaches its debt limit. At this point, no more bonds may be issued until part of the debt is retired or the tax base increases. However, communities at their debt limits may benefit by reviewing assessment practices and procedures. If assessed valuation can be legitimately increased, it will automatically provide more bonding capacity.

7b Can you get special permission to assume more debt?

In several states there are procedures by which school districts that have reached their debt limits can ask the state for special exceptions to issue more bonds. Such procedures are designed primarily for areas where the tax base is rapidly increasing and would clearly permit the assumption of additional debt. To find out if such procedures are available, contact your legal counsel, state school authorities, or state attorney general. If there are no established procedures, you may consider asking your state representatives about the possibility of special legislation enabling exceptions to the debt limit.

7c Does your state have a loan program?

Fourteen states operated loan programs during 1970:

Arkansas	Indiana	North Carolina	Wisconsin
California	Maryland	North Dakota	Wyoming
Connecticut	Michigan	Ohio	
Illinois	Minnesota	Virginia	

7d Do you qualify for a state loan?

This can be determined only by the officials of your state loan program, acting on knowledge of the specific case. In general, loan programs are intended to provide an alternative source of cash for school districts unable to sell bonds in the open market. This may include school districts near their debt limit, districts with poor credit ratings, and in some cases, school districts that cannot demonstrate their present ability to repay loans.

All 14 operational loan programs, except Michigan, provide loans for capital outlay purposes. Michigan's program covers interest only.

7e Are the loan terms more favorable than selling bonds in the open market?

The regulations governing state loan programs make it unlikely that you will ever have a choice between the program and a general bond sale. But if you do have this choice, there are important factors to consider.

First is the available interest rate. The impact of interest rates is suggested in section 8M. In general, state loan programs offer more favorable interest rates. Moreover, these rates are known in advance, whereas the rates paid on bonds are not known until the bonds are actually sold. However, a qualified bond counsel should be able to predict the rates closely. Moreover, it is possible to choose either loans or bonds if the school district reserves the right to reject bond bids that exceed the loan rate.

A second factor is administrative complexity. You may be able to get verbal assurances from state officials that a loan will be approved before you invest time and money in making the application. However, a bond sale involves unavoidable preliminary expenses of time and money, without guaranteeing that the bonds will actually be sold.

Third, the state loan program may offer important options such as refinancing of the loan in cases of financial distress. In contrast, if a community fails to meet bond obligations, it faces financial disaster.

7f Does the loan cover 100% of costs?

Loan programs vary: in some states, 100% loans are made only to school districts that have used up their bonding capacity. In other cases, loans are supplemental. The school district sells what bonds it can. Loans make up the difference.

7g Can you sell bonds on the open market?

Even when bond issues pass at elections, school districts may find themselves unable to market the bonds. Bonds are bought by investors for only one reason: to earn interest. How much interest they expect to earn depends on several factors.

First is the money supply. As money becomes more scarce, people compete for capital and bid up the interest rate in efforts to attract capital.

Second is tax status of the investment. A tax-exempt investment (as most school bonds are) is often more attractive than a taxable investment earning much higher interest, since the net earnings may be comparable.

Third is the risk in the investment. This is directly proportional to the fiscal soundness of the district issuing the bonds. One measure of fiscal soundness is the ratio of present indebtedness to debt limit. Districts heavily in debt may be regarded as poor risks and may have to pay higher interest rates. Districts with extremely poor credit ratings may find it impossible to market bonds at any price.

Another factor affecting bond sales is the interest rate ceiling. The majority of states have legal ceilings on the interest payable on bonds.

In tight money markets where interest rates on alternative investments are higher than the legal ceiling, bonds may also be unsalable. At this point, a school district may attempt "goodwill" sales to local financing institutions; but except in large cities, few local institutions have the money to purchase very large issues.

Opinions on the quality and expected interest rates for school bonds can be obtained from qualified bond counsels before attempting a bond election. You may find that under present marketing conditions the election would be futile because the bonds could not be sold.

7h Will the voters approve the bonds?

Since bond obligate future tax revenues, school bonds are uniformly subject to voter approval. However, in many areas there are restrictions on who can vote. For example, only property-owners may be eligible where bonds are retired with property taxes. In other cases, up to a two-thirds majority may be required.

These restrictions can make passage of bond issues difficult. Many property holders have no school-age children and have little interest in schools. On the other hand, many interested parents, particularly young parents and poor parents, may not be eligible to vote because they are not property owners. In addition, all kinds of voters are resisting increased taxes in any form. As a result, bond issues are being defeated in record numbers.

A large number of bond-election failures are attributed to these factors. Consequently, laws governing such elections have been challenged in several courts on the basis of the Supreme Court's "one-man, one-vote" ruling (Baker v. Carr). Court decisions have not yet changed the situation significantly. However, should these changes occur, school districts now unable to pass bond issues will have a better chance to pass them in the future.

Not all bond-election defeats are attributable to such political and legal problems. In many cases, bond issues are turned down by voters simply because the school system does not adequately demonstrate the need for additional facilities. In order to prove such a need, a school district should be prepared to answer the following:

1. Are present facilities up to standards? Do they meet building codes and state school requirements as well as generally accepted standards for education? If not, is it more economical to build a new facility or renovate the old one?

2. Are present facilities overcrowded? If so, have you examined and tested organizational changes, new scheduling, or curriculum changes that might relieve overcrowding? Is the addition of new space the only choice? Will future population shifts relieve or increase this overcrowding? Do you have adequate population projections to support these conclusions?

3. Have you carefully planned and estimated costs of additional construction? Many bond issues suffer at the polls simply because the scope and cost of proposed construction have not been carefully planned and explained.

4. Have you made clear the implications of defeat of the issue? If the need is inevitable, such as replacement of a totally obsolete facility, then delay in passing the issue will only mean a higher future tax bill since construction costs will in all likelihood continue to escalate a minimum of 3% per year. In some locales, costs have escalated up to 15% per year. However, also be aware that your tax base, and the taxpayers' income, will also increase in the future. In situations where the tax base is expanding rapidly, more construction may be accomplished later on at a lower tax rate, even though construction costs have increased. Building now simply to avoid inflation may not always be a valid strategy.

5. Have you made these facts clear to the public? School districts cannot actively campaign for passage of a bond issue. But they can make sure that the basis of their request, and the facts behind it, are made available to the public well in advance of the elections.

For additional information: Case Studies C, I
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8 Leasing

There are two distinct kinds of leasing programs, each with its own objectives: short-term and long-term.

Short-term or temporary leasing programs are used by school districts to alleviate space shortages caused by unexpected population shifts, delays in new construction, or changes in school curricula and organization. A typical solution is to place relocatable or temporary structures on the school site until the situation corrects itself, or until a permanent solution is found. If the need for space is temporary, the most economical solution may be to lease or rent it. When no longer needed, the space would be returned to the leasing organization.

Long-term leasing programs usually intend that the school district will lease the space until it can afford to purchase the building, or until the building is paid for; the building will then become school district property. The building will be designed, built, and used as a normal, permanent facility. Such leasing programs are a new way to finance permanent construction.

Long-term leasing programs are attracting a great deal of interest from educators all over the nation. In particular, they attract the interest of school districts that may have reached debt limits or cannot pass new bond issues at the polls. These and other legal-political problems may have made it impossible to build new schools.

Leasing is a popular option (perhaps the only option) in such cases, because leasing programs can often bypass these political and legal constraints.

Most leasing programs follow a standard pattern. A "third-party" organization assumes responsibility for the design, construction, and financing of a new school facility. The third party leases this facility (usually on a year-to-year basis) to the school district. Because the lease is for only one or two years and does not involve acquisition of capital equipment, the lease costs may be paid with operating funds. There is no long-term commitment involved, and therefore no effect upon the present indebtedness of the school system. However, there is usually a purchase option in the lease that allows the school district to buy the property at any time for the balance outstanding on the mortgage. When the mortgage has been retired, ownership of the school passes to the tenant school district.

In the end, the school district owns a school which in reality it has purchased on a time-payment plan. Yet it has done this without assuming any long-term debt. Except in locales where the operating budget is approved by voters, the school system can make such commitments without referendum to the voters. For these reasons, school systems that cannot finance additional space through normal channels may be able to acquire almost unlimited space through leasing programs.

8a Is leasing legal in your state?

No state unconditionally prohibits leasing, but several have laws regulating it. In other states, the legality of leasing may not be clear because the issue has not been tested.

In states where laws have been established or where legal tests have been conducted, the legality of leasing appears to hinge around the term or duration of the lease. A short-term lease, which does not obligate future governments by obligating future uncollected funds, is generally regarded as a legal current expenditure, payable with operating funds or capital funds. This is important to school districts short on capital funds, but which have adequate operating budgets. On the other hand, any lease which obligates future funds would generally violate fiscal statutes, and therefore be illegal.

In general, these legal factors rule out long-term leases unless they are either approved by referendum or specifically permitted by law. If school districts cannot sign long-term leases, the leasing organization may have difficulty in financing construction because the investor has no assurance that the school district will continue to make lease payments. For these reasons, some states have passed special laws which help reduce risks to investors. For example, California permits seven-year leases on temporary facilities, provided that cancellation of the lease does not create any immediate debt. In effect, such a lease is a one-year lease with options to renew for up to six additional years. This enables the district to signal its intention to lease over a longer term, without obligating it to do so in fact.

Indiana has a program which in effect guarantees payments of interest and principal on Revenue Bonds issued by non-profit leasing organizations.

Florida enables school districts to take 30-year leases by backing them with Motor Vehicle License Revenues—which is legal in Florida by virtue of a special constitutional amendment.

It is important to know what laws your state may have on leasing school space. If your legal counsel does not know, you may check with the state school authorities or the state attorney general's office. If there are no specific laws, then attempt to determine if there are any legal precedents. Voters in some states without specific laws have interpreted leasing as an attempt to evade fiscal controls on school spending by avoiding referendums on school construction. Such voter reaction has resulted in suits against the school district, out of which the legal precedents have arisen. While the large majority of such precedents are favorable to leasing, it would obviously be desirable to avoid such a test.

8b Can you lease from a building commission?

Some large cities have found it advantageous to form separate organizations to build and operate buildings for other government agencies. These building commissions provide complete ranges of building services to the using agency, including financing, design, bidding, construction and sometimes maintenance and operation of the facilities.

Some building commissions may be empowered to use the general bonding capacity of the city. Others may have special powers to issue revenue bonds. These bonds are similar to general obligation bonds, except that they are backed by pledges of revenues earned from the facility itself. The revenues, in this case, are lease payments from the using agency to the building commission.

Some cities are using such agencies to build schools, which are then leased back to the school district. The building commission works with the school district in establishing the program. The building commission may hire educational consultants to assist in this phase. The commission may design the facility using in-house staff, or may retain architectural services. Bids are taken following public bidding procedures. When bond financing has been secured, contracts are awarded and the facility is built. The commission then leases the completed facility to the school district. The commission may or may not provide maintenance services, and may or may not pay operating costs. Lease income gives the commission the ability to pay off the bonds. When the debt is retired, the school facility may either be turned over to the school district, or may be retained by the commission and leased at reduced cost.

8c If you are an independent district, can the city or county build and lease to you?

In at least one case, city government used its authority to issue revenue bonds to build and lease a school to an independent school district.

8d Can you lease from a nonprofit corporation?

Some school districts use specially created nonprofit corporations for financing, building, and leasing schools to the school district. While a school district cannot form such a corporation, any group of interested citizens (which might, if legal, include members of the school board) can form the corporation. Stock is sold to cover temporary operating expenses or to satisfy minimum capital requirements in the state. The corporation then seeks its nonprofit qualification from the U.S. Internal Revenue Service and state taxing authorities. For this, the corporation must show it will be dedicated to the public interest, must never pay dividends on stock, must reinvest earnings in the public interest, and must place its work, inventions, etc., in public domain. In return, the IRS declares the organization tax-exempt. In the case of school leasing, nonprofit corporations have the power to build, and the nonprofit status helps reassure the public that the corporation will act in the public interest.

The nonprofit corporation usually works in the same manner as a building commission in providing a school facility, with some exceptions. First, it will not usually have in-house design or other services, and will always hire these services. Second, since it is not officially a public agency, but is a quasi-private corporation, it need not observe public bidding procedures. The nonprofit corporation can therefore negotiate bids; or can hire package building services; or can use other time and cost saving procedures as it sees fit. Finally, it has the option of using revenue bonds, commercial notes, or commercial mortgages as financing instruments. The nonprofit corporation may have difficulty in issuing revenue bonds unless the bonds are backed by the school district, the state, or other authority. Similarly, it may have trouble securing commercial loans without such guarantees. The absence of long-term leases works against such loans, since the investors have no guarantee that the school will continue to be leased from the nonprofit corporation.

The first problem in setting up a nonprofit corporation will be finding a group of citizens willing to form the corporation. In some cases, it may be legal for members of the school board to act in such a capacity; or, it may be possible for other government officials to form the corporation. These persons would likely be directors of the corporation, but would not serve in any operating capacity. However, as directors, they have legal liabilities that should be carefully defined for them. Your counsel will know what these liabilities are in your state.

The steps in forming a nonprofit corporation are not complicated, but are best supervised by a qualified attorney. Usually, an organization meeting is held to draw up a corporation charter. The charter states (and limits) the purpose of the corporation; designates its officers; and sets forth the working rules. Stock certificates are issued to the shareholders, and their capital placed in a bank account. The charter and evidence that the corporation has the required minimum capital is filed with the state. After the state issues a corporation franchise, a *bona fide* private corporation exists.

The next step is to apply to state and federal tax authorities for permission to operate as a nonprofit corporation. This step is complicated and requires the services of a qualified corporate attorney. There is no guarantee that nonprofit status will be granted, regardless of what the charter may say, or of the intentions of the shareholders. If it is not obtained, the corporation can be immediately dissolved and the capital returned to the shareholders.

8e Can you lease from a private organization?

Most commercial leasing companies offer school districts a package deal that is a single contract covering design, financing, and construction of the school. However, these deals vary in internal organization.

Some package dealers are primarily manufacturers of building components, products, or prefabricated structures, such as classroom modules. A contract with such a firm implies use of its building products or systems. The company may be able to handle design and financing as well; or it may form a consortium with architectural and engineering firms, mortgage houses, and other outside talents.

Some package dealers are primarily general contractors. Their firms may provide in-house design services, or may subcontract them. These firms are not committed to building in one particular way, and will sometimes associate with prefabricators for a particular job.

Another type of package dealer provides about the same services as a developer—general coordination and management of the project with major services subcontracted. However, there is no fixed team established in advance, and the school district can participate in selecting architects, contractors, etc.

It is important to determine what kind of private leasing group you want to deal with because the services and advantages vary considerably. Most organizations claim to save time and costs because they are a coordinated team. This may be true with experienced package dealers, but temporary alliances of separate firms without extensive experience as a team may be less effective.

Because private construction operations are not bound by public procurement laws, they are able to use time and cost saving procedures such as negotiated bidding and fast-track scheduling (where carefully-phased planning and construction proceed simultaneously). Private organizations unencumbered by public construction procedures may save money on equipment and materials purchases. However, such savings can easily be offset by high interest rates paid by private organizations for commercial notes and mortgages for financing. (See Notes on interest rates: 8M)

Depending upon interpretation of applicable local laws, you may be able to select and deal with only one private leasing corporation. If so, look closely at the firm's record. How many schools has it built in this manner? What do former clients think of the firm? Have time and cost schedules been met?

If you are uncertain about negotiating with a single firm, you can also organize competitive bidding among private leasing companies. Such a competition can be based on firm educational specifications accompanied by space programs and standards for design and construction. The firms may then compete for the total design-build package by submitting design and cost proposals covering the total project. Competition may also be held in more than one stage to first narrow the field through design presentations, and then a price competition for the final award. This may encourage more accurate costing and will also give you additional opportunities to refine the design to meet your needs. Alternatively, you might elect to base competition for construction and leasing on a fixed design. This would not permit the design costs to be included in the lease financing and would tend to reduce some advantages inherent in package leasing.

8f Can you establish workable procedures for site acquisition?

Leasing programs raise special problems with site acquisition, clearance, and construction. When a school district acquires a site, it may have to use public acquisition procedures. But a leasing organization may have to acquire a site through normal commercial channels, which may increase costs.

If the school district owns the site, problems may arise in arranging for the leasing organization to build on school land. Several solutions to these problems have been developed. One is to sell the entire site to the leasing organization. However, if the leasing organization owns the entire site, this may create problems with school insurance during occupancy, e.g., liability insurance on play areas to avoid this, the school district may sell or lease only the ground to be occupied by the building.

If the leasing organization has rights only to the land occupied by the building, the leasing organization might not have rights to build site improvements such as walks, drives, and play areas. The leasing organization might donate such improvements to the school district, whereupon the school district could permit the corporation to build on public land for purposes of enabling the donation. Alternatively, the school district may pay for such improvements out of proceeds from sale or lease of the land to the leasing organization. Either way, the cost of site improvements will still be included in lease payments. The same procedures might be used for site clearance.

8g Can you establish workable procedures for programming?

Educational and architectural programming of leased facilities can be handled in two ways.

If you are dealing directly with only one leasing organization, that organization can retain educational consultants, architects, and others needed in programming the facility. The cost of such services can be included in the lease payments. This reduces front-end costs to the school district. However, the leasing organization may require reimbursement for such services if the project is not built.

Alternatively, the school district can do the programming itself. This is required when a commercial leasing organization is to be used and the school district decides to ask for competitive bids from different leasing groups. A detailed set of programs and criteria are required to make sure the bids are comparable.

8h Can you establish workable procedures for design of the school?

Since the leasing organization is the legal owner, it usually provides architectural and engineering services and assumes responsibility for obtaining approvals from code agencies, state school authorities, etc. However, since the school district is the final user, it will naturally want to be closely involved in the planning process. Procedures for this should be carefully worked out between the two parties.

If the school district calls for competitive bids on the lease package from several private companies, the competition may include design competition as well as price competition (see section 8E, 8G).

8i Can you establish workable procedures for bidding and construction? 26

Bidding for leased facilities varies with the type of leasing organization used in the program.

Building commissions may be required to follow public competitive bidding procedures similar to those used by school districts in conventional building programs.

Nonprofit leasing organizations, since they are not a public agency, may either take competitive bids in the usual manner or elect to negotiate bids. In negotiation, prices are set by agreement between the general contractor and the leasing organization. If desired, the general contractor may take competitive bids on one or more subcontracts under the supervision of the leasing organization. Negotiation may offer important advantages. First, the contractor can provide cost advice during design. Second, it saves time since prices are developed as the design progresses without waiting for competitive bids.

Private leasing organizations usually serve as general contractors. They may negotiate subcontracts or take competitive bids. A school district can also ask the contractor to take competitive bids on subcontract work. If the district wants a broader range of competition, see section 8E.

8j Can you establish procedures covering operations and maintenance?

In most leasing programs, the school district is responsible for all maintenance, operations, repairs, equipment replacement, renovations, and additions. In short, the leasing organization provides only a building, and the lease payments cover only the repayment of principle, interest, administrative and development costs, taxes, and insurance and profits (if any).

There are several reasons for this. First, operating and maintenance costs are difficult to predict and control; including them in the lease may increase the financial exposure of the leasing organization. Second, most leasing organizations are not equipped for such programs, but most school districts are experienced with operating maintenance programs. Third, it is extremely difficult to develop contracts covering maintenance. Problems such as defining the difference between normal wear and abuse are difficult to overcome. Similarly it is difficult to define standards of maintenance.

8k Can the leasing group finance the construction?

Different types of leasing organizations will finance the construction in different ways.

Building commissions sometimes use the city's general bonding authority, but where leased facilities are being built it will more often use revenue bonds. Revenue bonds are similar to general obligation bonds, except that they are backed only by the pledge of specific revenues, i.e., income from the leases.

Nonprofit leasing organizations cannot use the school district's bonding authority. Instead, they may issue their own revenue bonds or debentures; or, they may obtain commercial notes or mortgages from banks, mortgage houses, or insurance companies. Theoretically, a nonprofit might also sell capital stock to finance construction, but this would be unlikely since the nonprofit cannot pay dividends on stock.

The private leasing organization usually finances construction through commercial mortgages. However, private leasing organizations could also use real estate investment trusts, syndicates, or other vehicles to provide working capital.

The interest rates paid on different kinds of financing vary widely. Since the impact of interest charges on leasing costs is considerable (see 8M), it is important to consider how the lease is financed. General obligation bonds provide the lowest interest rates, primarily because they are more secure, and they are tax-exempt. Revenue bonds command about 1% to 2% higher interest because of increased risk. Commercial financing will bear considerably higher interest rates, unless special rulings can be obtained from IRS declaring the loans tax-exempt. This may be possible because the final beneficiary of the loan is a public agency. If tax-exemptions can be obtained, the interest rates on commercial loans can be comparable with GO bonds.

The ability to secure financing on leased facilities and the rate at which interest is paid varies with the security of the lease itself. Short-term leases are regarded as insecure since there is no guarantee that the facility will be occupied. Several states have therefore enacted laws enabling long-term leases, and/or guaranteeing payments of principal and interest on bonds, etc. See 8A. It may also be possible to sign a long-term lease if the question is submitted at referendum. Since state laws vary widely on this matter, check with your legal counsel or the state attorney general.

Some nonprofit leasing organizations have been empowered to generate income on their own to reduce financial requirements. These include sale of air rights (see 6B), and construction of rentable space (see 6C).

8I Can you afford the lease payments?

You may use current funds or operating funds to make lease payments since leasing does not involve acquisition of capital equipment. Therefore, it may be possible to make lease payments with operating funds. This is highly advantageous to school districts who have adequate operating budgets but who are short on capital funds. However, handling lease payments in this way will make per-pupil operating expenses appear much higher, compared to school districts that do not lease. In addition, some states do not provide operating aid for lease payments if the lease contains an option to purchase.

Some school districts that are short of operating funds have obtained legislation to pay lease costs with special levies imposed without referendum. Such legislation may already exist in the form of special taxing authority used by other government agencies.

A third option is the possibility of a special assessment district. It is often legal for voters to create a special assessment district, or special tax district, where the voters within that district agree to tax themselves for a service provided within that district. Such a district might be formed around a leased school, with a special levy passed to support lease payments.

The annual cost of leasing, and therefore the amount that must be budgeted, depends upon several factors: the cost of the facility, the form of long-term financing on the facility (and hence the interest rates), and the term of the financing. Usually, lease payments cover only the principal and interest paid by the leasing organization during each leasing period, plus administrative costs and profit, if any. These factors are closely related to the type of organization from which you choose to lease.

8m Notes on the impact of interest rates

The different types of financing instruments bear different interest rates. General Obligation bonds usually sell for between 3% and 6% net interest; revenue bonds usually add a point or two (4% to 7% is typical); and commercial loans, the most expensive of all, range from 7% to 14% or more. What determines this? First is the credit rating of the leasing organization and the school district lessee; this is also related to the lease security, i.e., the term and duration of the committed lease and the general money market.

Another major factor is the tax status of the loan. The IRS may declare certain loans tax-exempt, as are GO bonds, because the final beneficiary of the loan is a school district. If this is possible, the interest rates may be cut by as much as 40% on commercial loans.

In considering the impact of increasing interest rates, consult the following table, which provides sample interest rates on a 25-year level-term commercial note for each $1000 borrowed:

Annual Interest Rate	Monthly Payment	Total Interest Paid	Total Principal and Interest Paid	Total Interest as % of Principal	% Increase in Interest Payments Over 6% Base
6%	$ 6.44	$ 932.00	$1932.00	93.2%	—
7	7.07	1121.00	2121.00	112.1	+ 20.2%
8	7.72	1316.00	2316.00	131.6	+ 41.2
9	8.39	1517.00	2517.00	151.7	+ 62.7
10	9.09	1727.00	2727.00	172.7	+ 85.3
11	9.80	1940.00	2940.00	194.0	+108.1
12	10.53	2159.00	3159.00	215.9	+131.6
13	11.28	2384.00	3384.00	238.4	+155.7

For additional information: Case Studies A, B, C, D, E, G, I, J
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CS/A New York City Educational Construction Fund

The New York City Educational Construction Fund is a public benefit corporation devoted to the construction of schools on combined occupancy sites with housing, office buildings or other suitable projects (the lessee of the non-school portion).

The predominant functions of the Fund are:

—To oversee planning, design, financing and construction of schools. Schools are financed with notes or revenue bonds.

—To retire these bonds with income obtained from:

a. Leasing or selling air rights and/or property rights of Fund-owned sites for the construction of joint occupancy buildings;

b. Tax equivalent payments from the air-rights lessee, who pays the Fund an amount equal to the real estate taxes normally paid to the city.

The combined total of this income to the Fund may more than offset the annual debt service on the school building. Between 10% and 30% of income is from air-rights leases; the remainder is from tax equivalent payments.

The Fund operates in the following manner:

1. The Fund receives title to land from the city. This may be city-owned land or land acquired by normal acquisition procedures. To date, it has usually been city-owned land. The city may also assume the responsibility for relocating tenants on the site, and/or clearing the site.

2. In return, the Fund agrees to provide school facilities built to Board of Education specifications.

3. The Fund designates a developer to undertake development of both the school and the non-school building. This may be a private developer acting on his own; or, if the non-school portion is to be FHA Section 236 housing or other forms of subsidized housing, the developer may be working with a sponsor group. With variations in procedure depending upon the type of non-school lessee, the developer secures plans, estimates, financing, etc., for the total project. The Fund closely supervises all this activity. The project plans are also reviewed and approved by appropriate city agencies.

4. When approvals are received, and when the Fund is assured of project feasibility, construction begins. The Fund provides interim financing for the school portion of the project. It obtains its funds for this financing by issuing Bond Anticipation Notes which are short-term notes whose security is the power of the Fund to sell bonds at any time. The interest payments on such notes are assured by the city. Such notes have been obtained at rates between 4.25% and 6.9%. At the close of construction, the contractor has been paid for the school. The Fund may then elect to issue long-term bonds to retire the short-term note. So far, the short-term notes have been left in force and the Fund's bond-issuing capacity has been unused.

5. When the project is completed, the lease on the school facility (at $1.00 per year) becomes effective.

The two most often cited advantages of the system are related. First, the combined occupancy increases land use and promotes desirable planning, e.g., schools and housing in close proximity. The second advantage follows from the first: the joint occupancy provides income which offsets the construction cost of the school building. However, do not assume that the system always provides "free school buildings". The main reason is that the joint-occupancy building may not always produce enough income for the Fund to cover its debt service obligations. For example, several sites include moderate income housing built under New York's Mitchell-Lama Law and/or FHA 236 interest subsidy programs. Since such projects usually require tax-abatement, the Fund's tax-equivalency payments are reduced accordingly. When this happens, the Fund's income may not be equal to debt-service obligations, and a deficit project results.

The Fund handles such deficits in two ways. First, it may use surplus funds (from other projects where income exceeds debt-service requirements) to offset the deficit.

Second, it has arranged options to the City to make up any such deficit on either an annual basis or on a lump-sum basis. On the latter basis, the Fund calculates the portion of the total debt it can pay off based on income; the City pays the remainder. This provides the City with fiscal flexibility, in that by choosing between the alternatives, it can also choose between using "expense" or "capital" funds.

In summary, the Fund can provide new schools at no capital outlay except the cost of sites, and without impacting the city's position vis-à-vis debt limitations. In every instance, the Fund actually reduces the cost of the school facility by generating compensating income. Moreover, the additional opportunities of joint-occupancy planning are valuable in themselves. Finally, many political advantages accrue, e.g., it can build schools without reducing available housing in a neighborhood.

CS/B Chicago Public Building Commission

The Public Building Commission of Chicago (PBC) is a municipal corporation established by the Illinois State Legislature in 1955. Membership consists of the Mayor, representatives appointed by the County Board, the Board of Education, the Chicago Park District, the Metropolitan Sanitary District, and six lay citizens. The commission is authorized to issue and sell revenue bonds for financing construction for any city agency that needs a building. Then it develops specifications with the agency and oversees the design and construction.

School construction was added to the PBC mandate in 1968. At that time the Board of Education found it difficult to fulfill the demand for new construction and maintenance of existing schools. Chicago had to replace over 100 schools built before 1900 and modernize many others. All this was estimated to cost more than $1 billion, so because normal financing procedures could not meet such a demand, 20 high-priority schools were put into the hands of PBC. Educational specifications were written by the Board and consultants, and the PBC took care of the financing, design, bidding and construction.

The State Legislature recently raised the legal interest ceiling on PBC revenue bonds from 6% to 7%. PBC leases the school buildings to the Board of Education, which pays the lease and principal costs from a property tax levied over and above the present building fund levy. An additional tax is also levied to cover the cost of operation and maintenance of these school buildings during the period of the lease.

For its management services during construction, the PBC adds 2% to the total project cost. PBC services are at present limited to 20 high-priority projects totaling about $210 million in construction. At the same time, the Board of Education is continuing its regular building program.

PBC services may have added minor costs to the 20 projects. First, revenue bonds may sell at higher interest rates than general obligation bonds used by the Board of Education. Second, planning costs may be higher because of increased needs for inter-agency coordination.

If costs are greater, the increase can readily be justified because PBC's services permit the construction of schools now that would otherwise certainly have had to wait. Since construction costs are rising much more rapidly than tax revenues, each year's delay can mean a significant reduction in the buying power of the School Board.

Following the model of the New York City Educational Construction Fund, the Board of Education and the PBC are exploring air-rights possibilities of joint occupancy of schools in residential developments, and the construction of schools over expressways and railroads.

CS/C Boston Public Facilities Department

The Boston Public Facilities Department (BPFD) serves as the city's construction agency for all public buildings. It was created in 1966 to build the city's schools, but it does not maintain or operate them. BPFD is a department of city government, not an independent authority. It can build schoolhouses with funds obligated by the City Council and approved by the Mayor. No referendum is required beforehand, but voters may petition against the obligation within 20 days of the mayor's approval. If there is no challenge, the city can issue General Obligation bonds and increase tax levies to meet them.

According to state law, the limit on obligations is 2.5% of assessed property valuations, as determined by the state. However, several special provisions substantially relax this limit. First, the state Emergency Finance Board has the power to approve specific loan orders up to 5% of assessed valuation. Secondly, the state has an aid-to-school-construction act which subsidizes the cost of school construction. Boston can usually qualify for about 40% of the cost of the school (excluding site costs) as a reimbursement. The state requires that the city finance such aid through General Bonds, and the state generally repays the city at the same rate at which the city retires the bonds (but not in less than five years). However, the state law permits financing of bonds covering this state aid independent of the legal debt limits. The city may also appeal to the Emergency Finance Board to permit the remainder of construction costs for state-aided schools to be financed outside the legal debt limits. Using still other provisions, the city may in the end finance up to 100% of construction costs outside of the legal debt limitations. E.g., in cases where school construction is aimed at resolving a situation of *de facto* segregation, state aid may rise to 65% of construction costs.

The BPFD possesses a number of unusual powers. It may grant itself exceptions to code and zoning regulations of the city (although it is governed by state building regulations). It may also buy and sell certain city property with the approval of the Mayor and transfer from one agency to another the responsibility for operating and maintaining particular buildings. The department also has the power to lease or sell air rights. It may also provide for joint tenancy between public agencies or between a public agency and a private organization. In one case, it has provided for joint occupancy between a school, a semi-private institution, and the Tufts-New England Medical Center. (The project involves joint occupancy of an elementary school, the Quincy School, community services, and housing for married medical students. The specific arrangement involves condominium ownership of the site between the city and the medical center.)

CS/D The Indiana School Building Corporation

The following description from *The Indiana School Building Corporation,* by W. Monfort Barr, is excerpted with permission. Reprints may be obtained from:

Office of Coordinating Secretary
Indiana University
Box E, Bloomington, Indiana 47401

"A stringent debt limitation of 2% of actual assessed valuation in Indiana makes it necessary for many school officials to use Indiana's nonprofit school building corporation act in order to obtain funds for school construction. The act was passed by the Indiana General Assembly in 1947, Chapter 273, and has been amended from time to time. The constitutionality of the act was soon challenged and received a favorable opinion by the Indiana Supreme Court. A local Indiana School Building Corporation erects a school building and leases it to a school district. The school district pays a fixed rental and eventually becomes owner of the building. Most Indiana school officials have heard of the nonprofit school building corporation; those who have not had actual experience with it are often at a loss as to procedural details.

"The first step is the formation of a nonprofit corporation having a Board of Directors of three or more members. Nondividend bearing stock is issued and sold to residents of the community. The total amount might be as low as $1,000. This stock will be redeemed when the building corporation is dissolved, but no interest will ever be paid upon it.

"The corporation will need to employ an attorney who will work with bond counsel selected by the corporation. The bonds which are sold will be bonds of the building corporation and will not be a direct obligation of the school corporation. The bonds will be secured by a first mortgage on the school building and site. A local bank will usually serve as trustee for handling the funds of the holding corporation.

"The building corporation purchases from the school board that portion of the site, including access, upon which the building will be erected. The building corporation hires an architect, gets bids, and arranges for construction. The building corporation offers a lease to the school corporation, the amount and terms of which will be fixed in conference with bond counsel. The lease will pay off the obligation, with interest due, in a pre-determined number of years. Statutory requirements govern many provisions of the lease and other proceedings. The school board agrees to pay a partial amount for the year in which the building is made available and to pay the semi-annual lease-rental payment on June 30 and December 30 each year until such time as the school board exercises its option to purchase the building. The option to purchase should be exercised as soon as all bonds and stocks can be redeemed and the building corporation terminated.

"The rate of interest in 1964 ranged from 3.1% to 3.9%. It is necessary to borrow funds enough to pay interest for the first year and a half or more because during construction no lease-rental payments will be received by the building corporation. This amount is included when the original bonds are sold. The bonds are sold, as are any other municipal bonds, by obtaining a bond rating, by preparing a prospectus, and by advertising the sale of the bonds in the proper newspapers."

In addition to the public corporation, a similar act was passed in 1957 permitting private corporations to build and lease schools to local school districts. These private corporations operate in essentially the same manner, except that they use private money instead of revenue bonds to finance construction. Insurance companies are the usual source of such funds. Apparently by special provision, interest income on such loans is tax-exempt for the mortgagor, thus permitting lower-than-normal interest rates. Depending upon the bond market, such rates may be favorable with respect to bond market rates.

CS/E Illinois School Building Commission

The Illinois School Building Commission builds elementary and secondary schools and leases them to small school districts for 6% of the capital cost of the building and furnishings.

No charges are made for administrative expenses or interest. Leases are made for one-year at a time with an option to renew. If a school district elects not to renew, the commission may lease the building for any other type of occupancy. On the other hand, when a district completes the full life of a lease, the title is transferred to the district.

The Illinois State Legislature established the commission and supports it with an annual appropriation which currently runs at $38.5 million. The legislature aimed to assist two types of neighborhoods: economically depressed urban areas and rapidly growing suburban areas. These two both lack the high-yield taxable properties, such as office buildings and industrial plants that normally contribute heavily to educational costs. A state law limits municipal indebtedness to 5% of assessed valuation.

In order to qualify for the services of the commission, a local school district must show that it cannot meet school building needs within its current bonding capacity. And, it must also pass a special tax referendum to pay the lease costs.

Because it builds a large volume each year, the commission is able to keep construction costs low. It recently completed a high school with carpeting, airconditioning, and furniture for $17 per sq ft. In an effort to maintain economical costs, the commission is developing a prototype school building that can be used in many of the small districts it serves. This prototype is planned to upgrade the quality of educational facilities in districts that used not to have the resources to develop their own educational programs.

CS/F The Quincy Elementary School, Boston

Part of an urban renewal block near Tufts-New England Medical Center was designated as the site of the new Quincy Elementary School. It was to be built by the Boston Public Facilities Department using city money with state aid. The remainder of the block was planned for married student housing for Tufts. It was to be financed by the Massachusetts Health and Educational Facilities Administration (MHEFA), a state-chartered bonding authority.

During early planning, projected school size increased from 300 to 800 students. If the desired one-level plan were built, the school would require the entire city block, thus eliminating the housing. Planners then suggested building the housing over the school. As the idea developed, other community facilities were added, such as day care centers, teenage centers, and Tufts-aided school health facilities.

While the design concept met with general enthusiasm, it posed several legal problems. For example, both building agencies required free title to their properties. Since the housing above the school would not touch the ground, MHEFA could not get such a title. On the other hand, it was not possible for the city to lease school space from MHEFA or any other agency, since it would not then qualify for state aid. As a result, condominium laws did not clearly permit public agencies to own condominium property. In addition, since condominium owners are liable for proportional shares of property administration costs, it was unclear whether the school district would be illegally obligating itself to future costs. These and other legal problems are currently being examined, and legislation is in process.

Pending resolution of these problems, the Boston Public Facilities Department will acquire the site from the Boston Redevelopment Authority and construct the school. Between $4 million and $5 million will be provided through city bonds (40%) and state aid (60%). An additional $4 million to $5 million will be provided through MHEFA bonds. A small amount of private financing may be added to build approximately 5,000 sq. ft. of commercial space in the complex. Each of these parties will acquire condominium ownership of parts of the property.

The Boston Public Facilities Department will pass ownership of the school portion to the city school system, as it usually does. MHEFA will retain its ownership until the 40-year bonds are retired, at which time ownership will probably pass to Tufts. In the interim, the condominium corporation will be administered by a board of directors consisting of property owners and representatives of the users. The exact mix of representation and the method of selecting directors has not yet been determined.

Ironically, the current developments in design tend toward a two-level school with a separate tower for housing. Should this become the final design, the condominium scheme may not be used.

CS/G Butte County, California (Oroville Region)

Section 15232 of the California Educational Code permits California's autonomous school districts to lease temporary or portable space for schools for up to seven years. This applies to districts where voters may have refused a bond issue for construction but where additional space is needed. The Butte County Junior College District had its first bond issue rejected, and so made this legal power the basis of leasing *all* the space and equipment (including athletic equipment and other soft goods) necessary to support nearly 4,000 students. Thus, this new community college came into operation with a minimum capital outlay.

The college started on a temporary site in Durham, California. (It will move to a permanent 260-acre site in 1973.) The temporary site, an abandoned high school condemned under provisions of California's Field Act, was leased from the local school district. Negotiations began for 26 modular building units, and eventually, an unusual leasing arrangement emerged in which the district handled the equipment purchase and simultaneously arranged bank financing through regular commercial bank sources.

The plan called for the bank to pay the vendor, and in effect become the lessor to the school district. However, federal banking regulations prohibit a bank from becoming an original lessor in such cases. Therefore, the district arranged for a private citizen to act as the lessor. He simultaneously signed the agreement leasing the equipment to the school district, and assigned this lease to the bank. This permitted the bank to finance the lease, but at the same time not act as lessor. To avoid further complications, the private citizen's role was well defined as a role of convenience, with no legal rights or obligations. The same role could have been filled by a nonprofit corporation similar to the nonprofit school building corporations now existing in several states.

Several factors made this approach possible. First and most obvious is the provision in the educational code which permits 7-year leases. However, the statute applies only to personal property; hence the limitation to temporary or portable structures, which may be classified as personal as against real property.

Second was the willingness of banks to finance the leases. Again, the 7-year lease provision helps because it appears to have more security than year-to-year leases. This, however, is not true since California courts have held in other cases that long-term leases are constitutional only so long as termination of the lease does not create an immediate present debt. Therefore, the districts have effectively the same rights of cancellation as with year-to-year leases.

Premature cancellation or default could, of course, leave the bank owning school property. To guard against this contingency, an unusual agreement was written between the bank and the modular unit manufacturer, in which the manufacturer agreed to buy back the modules from the bank in the event of premature lease termination. (This in turn is made possible by a strong resale market for used modules.) This specific agreement might be the key to the operation of the system in states where only one-year leases are possible.

CS/H Inner Harbor Campus, Baltimore Community College

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The proposed Inner Harbor Campus will be located in a dense commercial district of a Baltimore redevelopment area. Some commercial properties will be razed, but the college will encourage the return of these services by providing 15,000 sq ft of commercial space on the ground floor of the new complex. The college expects to let a professional management group handle the rentals. Tenants will be asked to provide work-study opportunities for the students.

If pending legal rulings are favorable, public funds raised through bond sales will help finance the commercial space. The college will have to resolve whether to make profits on the rentals and use the proceeds for other expenses, or whether to only break even on rentals in the interest of better community relations.

CS/I Bowling Green, Kentucky

Statutory limits on interest rates caused the Bowling Green Independent School District to adopt an unusual leasing plan. Although the school district had bonding authority from a previous election, bond bids in neighboring school districts indicated that the district could not sell the bonds within the legal interest ceiling. So, the school district and the city agreed that the city would finance the school with revenue bonds and lease it to the school district. A friendly suit was arranged in state courts to test this use of the city's bonding authority. The court ruled favorably. The city then held the required referendum on the bond issue, which passed, and the school is now occupied.

An unusual feature of Kentucky law may have acted in favor of this plan. In Kentucky, the independent school districts normally issue bonds, but ownership of the building is assigned to the city served. Thus it is common to have city-owned schools operated by independent school districts.

CS/J State of Florida: State-Supported Leasing Programs

Florida state law permits local school districts to enter into lease or lease purchase agreements with either a state entity known as the Florida Development Commission or with private developers. The law covers the rental of new or existing school facilities. The unusual feature of the act is that the lease period may extend up to 30 years. However, the law stipulates that for any lease in excess of two years, the district may not use any form of *ad valorem* taxation to pay the lease costs. Instead, the state uses Motor Vehicle Licensing revenues to pay the local districts' costs. For such long-term leases, the local school district is backed by a state-supported pledge of funds. It is apparently the use of this source of revenue which permits such long-term leases to be signed without affecting current indebtedness.

Since the program is only six months old, no leases have been executed under this program.

Use of these leases will probably increase the cost of schools because of higher interest rates associated with the leases. However, the program is designed to service communities that must have additional space even though their bonding power has been exceeded. State approval is required for communities to use the program, and all facilities leased under it must meet state requirements.

CS/K Pontiac, Michigan: Human Resources Center

The Center opened in late 1971 with a wide range of community facilities integrated in the same building complex that houses an elementary school. Community facilities include health, recreation, cultural, adult education, in-service teacher training, and restaurants.

The city obtained more than $1.6 million from HUD's Neighborhood Facilities Program to assist with financing the project. But before the federal grant could be accepted, Michigan law had to be amended to enable the school district to receive the funds.

The grant enabled the school district to construct the additional facilities which are leased to other users. As a result, the school's educational program is broadened and brought closely in line with total community needs and resources.

Appendix

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The following publications are available from EFL, 477 Madison Avenue, New York, N.Y. 10022.

Bricks and Mortarboards. A guide for the decision-makers in higher education: how the colleges and universities can provide enough space for mushrooming enrollments; how the space can be made adaptable to the inevitable changes in the educational process in the decades ahead. (1964) $2.00

SCSD: The Project and The Schools. A second report on the project to develop a school building system for a consortium of 13 California school districts. (1967) $2.00

Design for ETV—Planning for Schools with Television. A report on facilities, present and future, needed to accommodate instructional television and other new educational programs. Prepared for EFL by Dave Chapman, Inc., Industrial Design. (1960) (Revised 1968) $2.00

Educational Change and Architectural Consequences. A report on school design that reviews the wide choice of options available to those concerned with planning new facilities or updating old ones. (1968) $2.00

Schools For Early Childhood. Ten examples of new and remodeled facilities for early childhood education. (1970) $2.00

Systems: An Approach to School Construction. Toronto, Montreal, and Florida projects and how they developed from the SCSD program. (1971) $2.00

Schools: More Space/Less Money. Surveys the alternatives for providing school spaces in the most economical manner. Includes extending school year, converting spaces, sharing facilities, open campus, etc. (1971) $2.00

High School: The Process and The Place. A "how to feel about it" as well as a "how to do it" book about planning, design, environmental management, and the behavioral and social influences of school spaces. (1971) $2.00

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College Students Live Here. A report on the what, why, and how of college housing; reviews the factors involved in planning, building, and financing student residences. (1962) $1.25

The School Library: Facilities for Independent Study in the Secondary School. A report on facilities for independent study, with standards for the size of collections, seating capacity, and the nature of materials to be incorporated. (1963) $1.25

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Air Structures for School Sports. A study of air-supported shelters as housing for playfields, swimming pools, and other physical education activities. (1964) $0.75

School Scheduling by Computer/The Story of *GASP*. A report of the computer program developed by MIT to help colleges and high schools construct their complex master schedules. (1964) $0.75

The High School Auditorium: Six Designs for Renewal. Renovation of little-used auditoriums in old and middle-aged schools to accommodate contemporary educational, dramatic, and music programs. (1967) $0.75

Middle Schools—controversy and experiment. (1965) $0.50

Schools Without Walls—open space and how it works. (1965) $0.50

The Schoolhouse in the City. An essay on how the cities are designing and redesigning their schoolhouses to meet the problems of real estate costs, population shifts, segregation, poverty, and ignorance. (1966) $0.50

The Impact of Technology on the Library Building. A position paper reporting an EFL conference on this subject. (1967) $0.50

Three High Schools Revisited: Andrews, McPherson, and Nova. (1967) $0.50

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Design for Paperbacks: A How-to-Report on Furniture for Fingertip Access. Physical solutions to the problems of displaying paperback books for easy use in schools. (1968) $0.50

On the Way to Work—five vocationally oriented schools. (1969) $0.50

The Early Learning Center. A Stamford, Conn. school built with a modular construction system provides an ideal environment for early childhood education. (1970) $0.50

An Investigation of Costs of Inexpensive Enclosures for Recreational Areas. Analyzes construction and operating costs for seven types of structures. (1969) Free

Transformation of the Schoolhouse. A report on educational innovations in the schoolhouse during the last decade, with financial data for the year 1968. Free.

Airconditioning for Schools. Cooler schools make better learning environments. (1971) Single copies free, multiple copies $0.25

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